



State of Idaho

Legislative Services Office

Individual Entity Audit Report

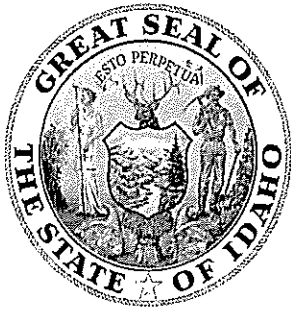
A communication to the Joint Finance-Appropriations Committee

IDAHO DEPARTMENT OF ENVIRONMENTAL QUALITY CLEAN WATER STATE REVOLVING FUND

FY 2011

Report OP24711
Date Issued: March 7, 2012

Serving Idaho's Citizen Legislature



Idaho Legislative Services Office
Legislative Audits Division

Don H. Berg, Manager

DEPARTMENT OF ENVIRONMENTAL QUALITY CLEAN WATER STATE REVOLVING FUND

SUMMARY

PURPOSE OF AUDIT REPORT

We have audited the financial statements of the Department of Environmental Quality (DEQ), Clean Water State Revolving Fund (CWSRF) for the fiscal year ended June 30, 2011, in accordance with auditing standards generally accepted in the United States of America. The purpose of our audit is to determine whether the CWSRF's financial statements are materially accurate and reliable, and that it complied with laws and regulations affecting fiscal operations.

CONCLUSION

We conclude that the CWSRF's financial statements are materially accurate and reliable, and fiscal operations materially comply with related laws and regulations. As a result, we issued an unqualified opinion on the CWSRF's financial statements.

FINDINGS AND RECOMMENDATIONS

There are no findings and recommendations in this report.

AGENCY RESPONSE

The Department has reviewed the report and is in general agreement with its contents.

PRIOR FINDINGS AND RECOMMENDATIONS

The prior report for fiscal year 2010 had one finding and recommendation.

Prior Finding 1 – Material errors in the financial statements were not detected by current internal control procedures.

The complete prior finding and recommendation is detailed on page 18.

This report is intended solely for the information and use of the State of Idaho and the Department of Environmental Quality and is not intended to be used by anyone other than these specified parties.

We appreciate the cooperation and assistance given to us by the director, Curt Fransen, and his staff.

ASSIGNED STAFF

Patrick Aggers, CPA, CFE, Managing Auditor

Chris Farnsworth, CPA, Managing Auditor

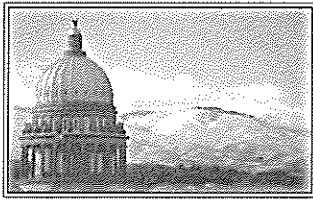
J.E. Bowden, CPA, CFE, In-Charge Auditor

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Legislative Services Office Idaho State Legislature

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Jeff Youtz
Director

March 7, 2012

Unqualified Opinion on
Basic Financial Statements

Independent Auditor's Report

Curt Fransen, Director
Idaho Department of Environmental Quality
1410 North Hilton Street
Boise, ID 83706

Dear Mr. Fransen:

We have audited the accompanying financial statements of the governmental activities, major fund, and the remaining fund information of the Idaho Clean Water State Revolving Fund (CWSRF) as of and for the year ended June 30, 2011, which collectively comprise the CWSRF's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the CWSRF's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business type activities, major fund, and the remaining fund information as of June 30, 2011, and the respective changes in financial position and its cash flow for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 7, 2012, on our consideration of the CWSRF's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered when assessing the results of our audit.

Mike Nugent, Manager
Research & Legislation

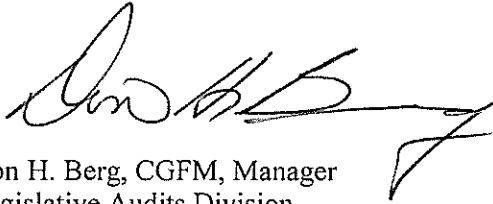
Cathy Holland-Smith, Manager
Budget & Policy Analysis

Don H. Berg, Manager
Legislative Audits

Glenn Harris, Manager
Information Technology

The Management Discussion and Analysis on pages 3 and 4 is not a required part of the basic financial statements, but is supplementary information required by the Government Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion thereon.

Sincerely,

A handwritten signature in black ink, appearing to read "Don H. Berg", with a long horizontal flourish extending to the right.

Don H. Berg, CGFM, Manager
Legislative Audits Division

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Idaho Clean Water State Revolving Fund (CWSRF) annual financial report presents our evaluation of the financial performance of the program for the State fiscal year (SFY 2011): July 1, 2010 through June 30, 2011.

Overview of the Financial Statements

The CWSRF basic financial statements include the Enterprise Fund financial statements and accompanying notes to the financial statements. The Enterprise Fund financial statements consist of the following elements necessary for fair presentation:

- Statement of Net Assets – This statement presents information on all assets and liabilities of the CWSRF, with the difference between assets and liabilities reported as net assets.
- Statement of Revenues, Expenses and Changes in Net Assets – This statement presents all revenues, expenses, and the changes in net assets of the CWSRF. The information in this statement is segregated into operating revenues, operating expenses, and non-operating revenues.
- Statement of Cash Flows – This statement details the categorical sources and uses of cash within the CWSRF, and provides a reconciliation of income to net cash provided by operating activities.
- Notes to the Financial Statements – This section details the financial activities, accounting policies and practices, as well as specific account information for the CWSRF.

These financial statements provide additional information to the specific operations on the CWSRF than that which is presented in the State of Idaho, SFY 2011 *Comprehensive Annual Financial Report (CAFR)*. The Idaho *CAFR* includes the CWSRF, the related but separate Drinking Water Revolving Loan Fund (DWSRF) which is also operated by the Idaho DEQ, and the Idaho Department of Water Resources loan program. Taken together, these three programs make up the Loan Fund as reported in the Idaho *CAFR*.

Financial Highlights State Fiscal Year 2011

- The CWSRF made \$47.8 million in loan disbursements to Idaho communities for wastewater projects, the largest amount ever for the Idaho CWSRF. The money used for these disbursements was from five primary sources: \$9.6 million from U.S. Environmental Protection Agency (EPA) CWSRF capitalization grants; \$2.0 million from Idaho matching funds to the capitalization grant; \$10.9 million from the EPA American Reinvestment and Recovery Act (ARRA); \$6.9 million from the U.S. Department of Education ARRA, and \$18.4 million from revolving funds (collected loan repayments and related revenues.)
- Loan repayments of \$12.6 million were received.
- Investments made by the Office of the Treasurer earned \$0.08 million in interest on CWSRF cash deposits remaining in the Idle Pool and \$1.5 million was earned by the Diversified Bond Fund.

Condensed Financial Information

	<u>FY 2011</u>	<u>FY 2010</u>
Total Assets	\$255,399,164	\$226,529,328
Total Liabilities	28,014	29,479
Total Net Assets	255,371,150	226,499,849
Operating Revenue	1,016,831	598,451
Operating Expenses	385,334	452,058
Non-Operating Revenue	28,239,804	15,539,048
Change in Net Assets	28,871,301	15,685,441

Analysis of Financial Position

The Idaho CWSRF grew by the largest amount in program history in SFY 2011, as evidenced by the \$28.9 million increase in net assets. This growth in assets was primarily due to the consumption of federal grants and the growth of earnings on increasing balances of loans receivable. During fiscal year 2011, EPA grants contributed \$20.5 million towards loan disbursements, Idaho matching funds contributed an additional \$2.0 million, and the U.S. Department of Education ARRA contributed \$6.9 million. The CWSRF earned \$4.6 million of loan interest revenue, cash earned \$0.08 million, and investments earned \$1.5 million.

Loans receivable as of June 30, 2011, was \$197.1 million, an increase of \$32.1 million from the prior year. During the year, the CWSRF made loan disbursements of \$47.8 million, while collecting \$8.7 million of loan principal repayments.

Investments decreased \$2.5 million to \$47.2 million. During SFY 2011, investments earned \$1.5 million, while \$4.0 million of withdrawals from investments were made to provide liquidity.

Cash decreased \$1.5 million to a balance of \$7.1 million.

There are no known facts, decisions, or conditions expected to have a significant impact on the CWSRF.

STATE OF IDAHO - DEPARTMENT OF ENVIRONMENTAL QUALITY
 CLEAN WATER STATE REVOLVING FUND
 STATEMENT OF NET ASSETS
AS OF JUNE 30, 2011

ASSETS	LOAN	ADMINISTRATIVE	
<u>Current Assets</u>	ACTIVITIES	ACTIVITIES	TOTAL
Cash	\$6,080,834	\$0	\$6,080,834
Cash - Loan Service Fees	0	1,048,024	1,048,024
Investments	47,223,785	0	47,223,785
Interest Receivable - Fund Balance	123,543	0	123,543
Interest Receivable - Loans	1,689,647	0	1,689,647
Fees Receivable - Loans	0	444,086	444,086
Interest Receivable - Fees	0	693	693
Loans Receivable	6,226,545	0	6,226,545
Total Current Assets	\$61,344,354	\$1,492,803	\$62,837,157
<u>Non-Current Assets</u>			
Loans Receivable	\$190,899,154	\$0	\$190,899,154
Interest Receivable	\$1,193,900	0	1,193,900
Fees Receivable - Loans	0	468,953	468,953
Total Non-Current Assets	\$192,093,054	\$468,953	\$192,562,007
TOTAL ASSETS	\$253,437,408	\$1,961,756	\$255,399,164
LIABILITIES			
<u>Current Liabilities</u>			
Payroll Payable	\$0	\$13,287	\$13,287
Operating Payable	0	11,009	11,009
Indirect Payable	0	3,718	3,718
Total Current Liabilities	\$0	\$28,014	\$28,014
TOTAL LIABILITIES	\$0	\$28,014	\$28,014
NET ASSETS			
Unrestricted	\$253,437,408	\$1,933,742	\$255,371,150
TOTAL NET ASSETS	\$253,437,408	\$1,933,742	\$255,371,150

The accompanying notes are an integral part of these financial statements.

STATE OF IDAHO - DEPARTMENT OF ENVIRONMENTAL QUALITY
 CLEAN WATER STATE REVOLVING FUND
 STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
 FOR THE YEAR ENDED JUNE 30, 2011

	LOAN ACTIVITIES	ADMINISTRATIVE ACTIVITIES	TOTAL
OPERATING REVENUES			
Contribution from Federal Government	\$0	\$319,243	\$319,243
Loan Servicing Fee Revenues	0	697,588	697,588
Total Operating Revenues	\$0	\$1,016,831	\$1,016,831
OPERATING EXPENSES			
Program Administration			
Personnel	\$0	\$265,377	\$265,377
Indirect Admin. Expense	0	100,041	100,041
Operating Expense	0	19,916	19,916
Total Operating Expenses	\$0	\$385,334	\$385,334
Operating Income(Loss)	\$0	\$631,497	\$631,497
NON OPERATING REVENUES			
Contributions from Federal Government	\$27,324,993	\$0	\$27,324,993
Contributions from State	2,000,400	0	2,000,400
Interest Earned - Idle Pool	73,647	0	73,647
Interest Earned - DBF	1,442,720	0	1,442,720
Interest Earned - Loans	4,573,328	0	4,573,328
Interest Earned - Loan Service Fees	0	7,261	7,261
Net Decrease in Fair Value of Investments	(2,909)	0	(2,909)
Loan Forgiveness	(7,179,636)	0	(7,179,636)
Total Non-Operating Revenues	\$28,232,543	\$7,261	\$28,239,804
Change in Net Assets	\$28,232,543	\$638,758	\$28,871,301
Net Assets - Beginning of Year	\$225,204,865	\$1,294,984	\$226,499,849
Net Assets - End of Year	\$253,437,408	\$1,933,742	\$255,371,150

The accompanying notes are an integral part of these financial statements.

STATE OF IDAHO - DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2011

	LOAN ACTIVITIES	ADMINISTRATIVE ACTIVITIES	TOTAL
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash Received from Federal Government	0	319,243	319,243
Cash Received - Loan Service Fees	0	367,412	367,412
Cash Payments - Administrative Expenses	0	(386,799)	(386,799)
Net Cash Provided by Operating Activities	0	299,856	299,856
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES			
Cash Received from Federal Government	\$27,324,993	\$0	\$27,324,993
Cash Received as State Match	2,000,400	0	2,000,400
Net Cash Provided by Non-Capital Financing Activities	\$29,325,393	\$0	\$29,325,393
CASH FLOW FROM INVESTING ACTIVITIES			
Loans and Interest Cash Flows			
Cash Received - Loan Interest Payments	\$3,884,021	\$0	\$3,884,021
Cash Received - Loan Principal Repayments	8,740,124	0	8,740,124
Cash Received - Loan Service Fees Interest	0	7,376	7,376
Loan Disbursements	(47,839,914)	0	(47,839,914)
Cash Received - Investment Interest	1,531,061	0	1,531,061
Sale of Investments	4,000,000	0	4,000,000
Purchase of Investments	(1,455,174)	0	(1,455,174)
Net Cash Used by Investing Activities	(\$31,139,882)	\$7,376	(\$31,132,506)
Net (Decrease) Increase in Cash	(\$1,814,489)	\$307,232	(\$1,507,257)
Cash Balance - Beginning of Year	7,895,323	740,793	8,636,116
Cash Balance - End of Year	\$6,080,834	\$1,048,025	\$7,128,859
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES			
Operating Income	\$0	\$631,497	\$631,497
Adjustments by Operating Activities			
Change in Payables	0	(1,465)	(1,465)
Change in Receivables	0	(330,176)	(330,176)
Total Adjustments	\$0	(\$331,641)	(\$331,641)
Net Cash Provided by Operating Activities	\$0	\$299,856	\$299,856

The accompanying notes are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization of the Fund

The Clean Water State Revolving Fund (CWSRF) was established pursuant to Title VI of the Federal Water Quality Act of 1987 (the Act). The Act established the CWSRF program to replace the construction grants program and provide loans at reduced interest rates to finance the construction of publicly owned water pollution control facilities. Instead of making grants to communities that pay for a portion of building wastewater treatment facilities, the CWSRF provides a flexible financing source that can be used for a variety of pollution control projects. Loans made by the CWSRF must be repaid within 20 years (30 years for some disadvantaged communities), and all repayments, including interest and principal, must be returned to the CWSRF. The money in the CWSRF is to be used for eligible purposes in perpetuity.

The CWSRF is in the process of being capitalized by the U.S. Environmental Protection Agency (EPA) through a series of grants beginning in 1989. States are required to provide an additional 20% of the federal capitalization grant as matching funds in order to receive a grant. As of June 30, 2011, Congress authorized the EPA to award \$140,241,715 in capitalization grants to Idaho. The State is required to contribute \$28,048,343 in matching funds to receive these capitalization grants.

The American Recovery and Reinvestment Act of 2009 (ARRA) provided the CWSRF with \$29,239,100 of additional funding with no required State match.

The CWSRF is administered by the Idaho Department of Environmental Quality (DEQ). The CWSRF does not have any full time employees. Instead, DEQ charges the CWSRF for time spent on CWSRF activities by DEQ employees, and the CWSRF reimburses the DEQ Fund for such costs. The charges include the salaries and benefits of the employees, as well as indirect costs allocated to the CWSRF based on direct salary costs. Employees charging time to the CWSRF are covered by the benefits of the State. The CWSRF is also charged indirect costs of the State through the cost allocation plan for general State expenses.

The financial statements are intended to present the financial position and results of the operations of the CWSRF, a component of the State of Idaho. These statements are not intended to present the financial position or results of operations for the Idaho Department of Environmental Quality, of which the CWSRF is a part.

Basis of Accounting and Measurement Focus

Enterprise funds, in accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, are required to apply applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: *Statements and Interpretations of Financial Accounting Standards Board (FASB)*; *Accounting Principles Board Opinions*; and *Account Research Bulletins of the Committee on Accounting Procedures*. In addition, an enterprise activity may apply all FASB statements and interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements. The CWSRF has elected not to follow FASB pronouncements issued after November 30, 1989.

The CWSRF presents its financial statements as an enterprise fund. Enterprise funds are reported using the economic resources measurement focus and the accrual basis of accounting. The State's central accounting system records transactions on a cash basis of accounting. The CWSRF financial records have been converted as necessary to an accrual basis. The accrual basis of accounting requires recording revenues when earned and expenses when incurred. The fund accrues revenues and expenses at year-end based on activities recorded sixty (60) days subsequent to year-end.

Operating and Non-Operating Revenue and Expenses

Operating and non-operating revenue and expenses are presented separately on the operating statement. Operating revenue and expenses result from transactions associated with the administrative activity of the CWSRF, for example, administrative expenses and contributions from the EPA and loan servicing fees for administrative costs. All other transactions are reported as non-operating revenue, such as loan disbursements, collections, interest earned, contributions from the EPA and the State for loan disbursements.

Cash

Pursuant to Idaho Code, all cash of the CWSRF is deposited with the Office of the State Treasurer. The State Treasurer is responsible for the investment of the cash balances of the State.

In accordance with the Clean Water Act and Idaho Code, all cash of the CWSRF is perpetually appropriated for program purposes.

Capital Assets

Capital assets are generally defined as land, land improvements, buildings, fixtures, equipment, and property under construction, and are recorded at cost. The CWSRF owns no land, land improvements, buildings, fixtures, or property under construction and has no plans to acquire any.

Loans Receivable and Interest Capitalization

Loan funds are disbursed to the local agencies as the agencies incur costs for the purposes of the loan and request loan disbursements from the CWSRF. Typically, interest is calculated from the date that funds are advanced. After final disbursement has been made, the repayment schedule identified in the loan agreement is adjusted for the actual amounts disbursed and interest accrued during the project period. At the loan closing, the loan recipient is given the opportunity to pay off any accrued interest during the construction phase or to capitalize the interest into the loan principal, subject to the available debt capacity of the loan recipient as stated in the loan award.

Management considers all loans to be fully collectible; therefore, no allowance for uncollectible accounts is made.

Indirect Costs - Specific CWSRF Liabilities

Certain liabilities, such as compensated absences, pension plan obligations, and commitments under non-capitalized (operating) leases are obligations of the Department of Environmental Quality and the CWSRF receives an allocation of these costs, either through direct expenses as incurred or through the application of a negotiated indirect rate.

For the year ended June 30, 2011, the CWSRF does not have separate specific liabilities for compensated absences, pension plan obligations, and commitments under non-capitalized (operating) leases.

State Match

Under Idaho Code, the State match is perpetually appropriated from the Water Pollution Control Account. The State is only required to deposit a cash match into the CWSRF when an actual cash draw from the EPA is made.

Loan Servicing Fees

To support the administration of the CWSRF in perpetuity, a loan servicing fee of 1% is assessed on the outstanding loan receivable balance. The fees are deposited to an account outside the CWSRF and will be used for administration costs of the program.

<u>Loan Servicing Fees</u>	
Beginning Balance – July 1, 2010	\$740,793
Collections	367,411
Interest Income – Loan Servicing Fee Account	7,376
Expenditures	(67,556)
Ending Balance – June 2011	<u>\$1,048,024</u>

NOTE 2 – CASH AND INVESTMENTS

The CWSRF participates in two of the State Treasurer's investment pools. In accordance with Idaho Code, Sections 67-1210 and 67-1210A, the State Treasurer invests in various types of investments, including certificates of deposit, repurchase agreements, securities lending, and federal, State, and local government securities.

The Idle Fund is an involuntary internal investment pool managed by the State Treasurer's Office on behalf of participants. Money not needed to meet immediate operating obligations is invested in the Idle Fund, which is unrated. The CWSRF has total deposits of \$7,128,858 in the pool. Deposits are stated at cost, which approximates market.

The CWSRF also participates in the Diversified Bond Fund (DBF), an external investment pool. This pool is sponsored by the State Treasurer's Office under the authority of Idaho Code, Sections 67-1301 and 67-2328. As of June 30, 2011, the CWSRF investment in the DBF had a fair value of \$47,223,785 with a weighted average maturity of investments at June 30, 2011 of 4.5 years. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. A copy of the State's *Comprehensive Annual Financial Report (CAFR)*, including the investment pool's financial statements, is available from the Office of the State Controller.

The Department has not adopted a formal investment policy that addresses credit and interest rate risk related to the Idle Fund and the DBF investments.

NOTE 3 – LOANS RECEIVABLE

Extent, Nature, and Terms of Financial Instruments

The CWSRF makes loans to qualified agencies for projects that meet the eligibility requirements of the Act. Loans are financed by capitalization grants, State match, and revolving funds. Effective interest rates on loans range between 0% and 4.5% and are generally repaid over 20 years (30 years for some disadvantaged communities) starting within one year after project completion.

Collateral

At the loan closing, the State of Idaho receives collateral, typically a sewer revenue bond, local improvement district bond; or promissory note, from the borrower. As of June 30, 2011, the Office of the State Treasurer held \$85,627,283 (at original face value) of bonds and \$45,170,773 (at original face value) of promissory notes as collateral for the Clean Water State Revolving Fund.

Loans by Category

Completed projects are loans in the repayment phase. Projects in progress are in construction or the disbursement phase. Loans that have been paid in full are excluded. Loans receivable at June 30, 2011, are as follows:

	<u>Loan Authorized</u>	<u>Principal Repayments</u>	<u>Remaining Commitment</u>	<u>Receivable Balance</u>
Completed Projects	\$155,240,636	\$36,511,368	\$0	\$118,729,268
Projects in Progress	<u>158,980,331</u>	<u>0</u>	<u>80,583,900</u>	<u>78,396,431</u>
Totals	<u>\$314,220,967</u>	<u>\$36,511,368</u>	<u>\$80,583,900</u>	197,125,699
Less: Amount Due Within 1 Year (Current)				<u>6,226,545</u>
Loans Receivable, Net of Current Maturities				<u>\$190,899,154</u>

The projected principal repayments in subsequent years are as follows:

<u>Year Ending June 30:</u>	<u>Amount</u>
2012	\$6,226,545
2013	8,152,267
2014	9,679,303
2015	10,182,228
2016	10,370,356
Thereafter	<u>152,515,000</u>
Total Loans Receivable	<u>\$197,125,699</u>

Major Loans to Idaho Agencies

As of June 30, 2011, the CWSRF had made loans to the agencies listed below that, in aggregate by agency, exceeded \$10 million. The outstanding balance of these loans represents approximately 67% of the total loan receivable, as follows:

<u>Local Agency</u>	<u>Authorized Loan</u>	<u>Outstanding Balance</u>
North Lake Sewer & Water District	\$34,361,552	\$27,909,457
City of Coeur d'Alene	28,000,000	23,703,761
City of Pocatello	22,630,315	16,947,157
City of Ammon	20,000,000	18,857,152
City of Chubbuck	19,848,782	16,952,087
City of Idaho Falls	18,150,000	0
City of Burley	16,928,564	15,043,208
City of Rigby	13,000,000	4,976,900
City of Driggs	10,650,000	0
City of Boise	<u>10,528,098</u>	<u>7,795,929</u>
Totals	<u>\$194,097,311</u>	<u>\$132,185,651</u>

The current loan amount includes projects in construction and projects in the repayment phase. Loans that have been fully repaid are excluded. As of June 30, 2011, principal repayments on completed projects still in the repayment phase were \$18,247,141, and remaining amounts to be disbursed on projects in construction were \$43,664,518.

NOTE 4 – INTEREST RECEIVABLE

The interest rate on loans ranges from 0% to 4.5%, and loans are generally repaid over 20 years (30 years for some disadvantaged communities) starting within one year after the project is completed. Details of loan interest receivable as of June 30, 2011, are as follows:

Interest Receivable by Category

Completed Projects	\$1,193,900
Projects in Progress	<u>1,689,647</u>
Total Interest Receivable	<u>\$2,883,547</u>

NOTE 5 – CONTINGENCIES

The CWSRF is exposed to various risks of loss related to torts, thefts of assets, errors or omissions, injuries to State employees while performing CWSRF business, or acts of God. The CWSRF maintains insurance (through the Idaho State Department of Administration, Bureau of Risk Management) for all risks of loss. The cost of insurance is included in the indirect costs charged to the CWSRF. There have not been any claims against the CWSRF since its inception in 1989.

NOTE 6 – CONTRIBUTED CAPITAL AND FUND BALANCE

The CWSRF is capitalized by EPA grants authorized by Title VI of the Act and matching funds from the State. All funds drawn are recorded as contributed capital from the EPA and the State. As of June 30, 2011, EPA has awarded capitalization grants of \$140,241,715 to the State, of which \$140,160,423 has been drawn for loans and administration of the CWSRF. The State has provided the required matching funds of \$28,048,343. The following schedule summarizes the capitalization grants awarded by Federal fiscal year, amounts drawn on each grant as of the balance sheet date, and balances available:

<u>Year</u>	<u>EPA Grant Amount</u>	<u>Total Draws at June 30, 2010</u>	<u>Draws During SFY 2011</u>	<u>Total Draws at June 30, 2011</u>	<u>Balance at June 30, 2011</u>
1989	\$4,577,200	\$4,577,200	\$0	\$4,577,200	\$0
1990	4,738,000	4,738,000	0	4,738,000	0
1991	10,343,215	10,343,215	0	10,343,215	0
1992	9,534,900	9,534,900	0	9,534,900	0
1993	9,431,000	9,431,000	0	9,431,000	0
1994	5,813,800	5,813,800	0	5,813,800	0
1995	6,007,800	6,007,800	0	6,007,800	0
1996	6,318,400	6,318,400	0	6,318,400	0
1997	6,576,800	6,576,800	0	6,576,800	0
1998	6,577,300	6,577,300	0	6,577,300	0
1999	6,577,900	6,577,900	0	6,577,900	0
2000	6,555,200	6,555,200	0	6,555,200	0
2001	6,496,100	6,496,100	0	6,496,100	0
2002	6,510,800	6,510,800	0	6,510,800	0
2003	6,467,800	6,467,800	0	6,467,800	0
2004	6,471,800	6,471,800	0	6,471,800	0
2005	5,243,500	5,243,500	0	5,243,500	0
2006	4,242,300	4,242,300	0	4,242,300	0
2007	5,207,300	5,207,300	0	5,207,300	0
2008	3,274,300	3,274,300	0	3,274,300	0
2009	3,274,300	3,274,300	0	3,274,300	0
2010	<u>10,002,000</u>	<u>0</u>	<u>9,920,708</u>	<u>9,920,708</u>	<u>81,292</u>
Totals	<u>\$140,241,715</u>	<u>\$130,239,715</u>	<u>\$9,920,708</u>	<u>\$140,160,423</u>	<u>\$81,292</u>

As of June 30, 2010 and 2011, the State match contributions were:

	<u>Total Match Provided at June 30, 2010</u>	<u>State Match Provided in SFY 2011</u>	<u>Total Match Provided at June 30, 2011</u>	<u>Available State Match Balance at June 30, 2011</u>
Idaho CWSRF	\$26,047,943	\$2,000,400	\$28,048,343	\$0

NOTE 7 – AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009

The American Recovery and Reinvestment Act of 2009 (ARRA) will provide the Idaho CWSRF with up to \$29,239,100 of federal funds, with no required State match. The ARRA funds will come from the following: \$19,239,100 from the U.S. EPA, and \$10,000,000 from the U.S. Department of Education.

The EPA ARRA funds came with numerous requirements including:

- 1) The projects selected were to be "shovel ready" and under contract by February 17, 2010.
- 2) Additional subsidization of projects in the amount of at least 50% of the ARRA grant. Idaho has chosen to provide principal forgiveness to meet this requirement.
- 3) Not less than 20% of the ARRA grant was to go to Green Project Reserve, defined as green infrastructure, water or energy efficiency improvements, or other environmentally innovative activities.

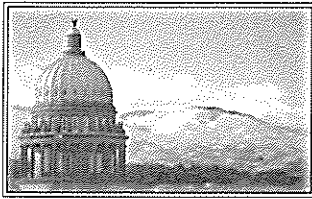
Additional information regarding the American Recovery and Reinvestment Act can be found at the http://www.deq.idaho.gov/water/arra/arra_water_projects.cfm and <http://www.recovery.gov/websites>.

Loan disbursements to qualified projects for incurred costs are necessary to collect these funds. As of June 30, 2011, \$14,264,741 (74.1% of available funds) of U.S. EPA ARRA and \$10,000,000 (100.0%) of U.S. Education ARRA loan disbursements have been made.

NOTE 8 – NORTH LAKE DEFAULT

North Lake Recreational Sewer and Water District (North Lake) has defaulted on CWSRF Loans 1899-09, 1899-16, and 1899-18. On June 14, 2011, North Lake did make \$541,405 towards repayment on Loans 1899-09 and 1899-16. These three loans remain significantly behind their repayment schedules.

DEQ is taking an active role in monitoring and assisting North Lake's efforts at securing repayments. The District Court has recently confirmed North Lake's statutory priority above other creditors in the Tamarack Resort foreclosure proceeding. Tamarack Resort comprises a majority of the local improvement district assessments in the three delinquent loans. On September 1, 2010, North Lake filed a claim against Tamarack Resort LLC for approximately \$36 million in the Tamarack bankruptcy action.



Legislative Services Office Idaho State Legislature

Serving Idaho's Citizen Legislature

Jeff Youtz
Director

March 7, 2012

Independent Auditor's Report on Internal Control over
Reporting and on Compliance and Other Matters Based
on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards*

Curt Fransen, Director
Idaho Department of Environmental Quality
1410 North Hilton Street
Boise, ID 83706

Dear Mr. Fransen:

We have audited the financial statements of the Idaho Department of Environmental Quality, Clean Water State Revolving Fund's (CWSRF) as of and for the year ended June 30, 2011, and have issued our report thereon dated March 7, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the CWSRF's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

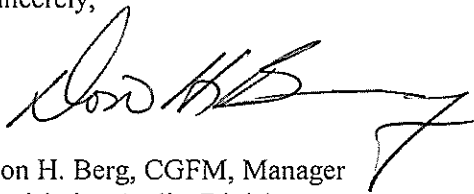
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies that are also considered to be material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the CWSRF's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Idaho Department of Environmental Quality and the Idaho Legislature and is not intended to be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read "Don H. Berg", followed by a long horizontal line and a large, stylized flourish.

Don H. Berg, CGFM, Manager
Legislative Audits Division

AGENCY RESPONSE



STATE OF IDAHO
DEPARTMENT OF
ENVIRONMENTAL QUALITY

1410 North Hillon • Boise, Idaho 83706 • (208) 373-0502

C.L. "Butch" Otter, Governor
Toni Hardesty, Director

March 7, 2012

Mr. Don Berg, Manager
Legislative Audits
Legislative Services Office
P O Box 83720
Boise, Idaho 83720-0054

Re: Audit Report – 2011 Clean Water Revolving Fund

Dear Mr. Berg:

The Department of Environmental Quality accepts the audit report.

If you or your staff have any further questions, please contact Dave Sande, CPA, Financial Officer.

Sincerely,

A handwritten signature in black ink, appearing to read "C. Fransen", is written over a horizontal line.

Curt A. Fransen
Director

cc: Dave Sande, DEQ-Fiscal Office

PRIOR FINDING AND RECOMMENDATION

PRIOR FINDING 1

Material errors in the financial statements were not detected by current internal control procedures.

RECOMMENDATION

We recommended that the Department review and strengthen the internal controls and processes for preparing financial statements and notes to reduce the risk of errors and omissions.

AUDIT FOLLOW-UP

The Department has implemented processes that strengthen internal controls for preparing financial statements and notes that reduce the risk of errors and omissions.

STATUS – CLOSED

APPENDIX

HISTORY AND STATUTORY AUTHORITY

The Idaho Clean Water State Revolving Fund (CWSRF) was established pursuant to Title VI of the Federal Clean Water Act of 1987. The CWSRF has been capitalized by a series of grants from the U.S. Environmental Protection Agency beginning in 1989.

PURPOSE

The Act established the CWSRF program to provide loans at reduced rates to finance the construction of publicly owned water pollution control facilities. Instead of making grants to communities that pay for a portion of building wastewater facilities, the CWSRF provides a flexible financing source that can be used for a variety of pollution control projects. Loans made by the CWSRF must be repaid within 20 years (30 years for some disadvantaged communities), and all repayments, including interest and principal, must remain in the CWSRF.

ORGANIZATION AND STAFFING

The CWSRF is administered by the Idaho Department of Environmental Quality (DEQ). The CWSRF has no full-time employees, but instead uses DEQ employees on a part-time basis. The part-time positions include the CWSRF's loan program manager, senior accountant, loan program specialist, lead loan officer, water quality analyst, six regional managers, and several staff and technical engineers.

Department of Environmental Quality
Director's Office

